

*Empowering
Ministry Through
Proven Asset
Management*

ucfocus

The Quarterly Newsletter of the United Church Foundation — An associated ministry of the United Church of Christ

CATHERINE WATERWORTH APPOINTED CIO

The Pension Boards-UCC (PB) recently announced that Catherine (“Kate”) Waterworth would succeed George Doty as Chief Investment Officer when he retires this summer. This position oversees the work of the seven PB professional asset managers who control portfolios of stocks and bonds worth over \$2 billion and an array of outside investment managers used by both the PB and UCF. About \$500 million of these assets are managed for over 1,000 local congregations and other UCC agencies that are participants in the United Church Foundation’s Common Investment Funds.

In place of our usual Q & A – Focus on Investing feature, UCFocus interviewed Kate to introduce her to our readers and to learn something about her views on investing.



UCFocus: Congratulations, Kate, on your selection for this position. Welcome to the United Church of Christ and to your new role leading our asset management group. This must be an exciting job transition for you!

Kate: Thank you. It is very exciting to assume this new responsibility, and to work with this team of dedicated investment professionals who are committed to delivering superior investment results to our constituents. Yet in some ways, it feels like I have been preparing for this job all of my life.

UCFocus: How so, Kate? Tell us a bit about yourself. We

know that you hail from Clearfield, Pennsylvania, but have been a resident of New York City for many years. We also know you graduated cum laude from Trinity College in Washington, D.C., and have studied at Oxford University and the University of Michigan in Ann Arbor. But where have you worked before this to prepare you for this job?

Kate: Most recently, I was a managing director at Neuberger Berman, LLC, a large investment advisory firm in NYC that has a diversified client base. My group managed a \$7 billion portfolio of fixed income assets. I also served on the asset allocation committee of the Financial

Advisory Services Group — a fund of funds manager. Prior to that, I worked for Continental Insurance Asset Management. They sent me to London for three years to oversee all of their European investment assets. And before that, I did several years of equity research for Wertheim & Co., Inc., an institutional investment advisory firm. I started my investment management career 30 years ago at Spencer Trask, which at that time was a specialty investment research shop.

UCFocus: In terms of previous clients, can you tell us anything about some of the institutions you served as an investment advisor, and

perhaps something about how their needs might have been comparable to those of our participants?

Kate: In the past, I have managed assets for other non-profit organizations such as UNICEF, New York Women’s Foundation, the Local Initiatives Support Corp. and many non-profit hospitals sponsored by various faith-based organizations. Even though these organizations had different mandates, they shared an underlying objective of maximizing total return in accordance with their individual investment policies and guidelines, many

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Electronic Funds Transfers Now Available

The UCF can now send funds to participants via an Electronic Funds Transfer (EFT), depositing funds automatically into their checking accounts. An EFT is processed through the Automated Clearing House system and thus “clears” the next business day as a secure bank-to-bank

transfer. This makes your money available for use sooner without requiring another trip to the bank.

Application forms for implementing this new service were sent to all participants with quarterly statements. If you misplaced your copy, give us a call toll-free at 877-806-4989, and we will send you another. Sign-up for UCF electronic funds transfers today.

Toll-free: 877-806-4989 • **Phone:** 212-729-2600
Fax: 212-729-2601 • **e-mail:** info@ucfoundation.org
website: www.ucfoundation.org
475 Riverside Drive, Suite 1020, NY, NY 10115

**UNITED CHURCH
FOUNDATION**

UCF Co-FILES EIGHT SHAREHOLDER RESOLUTIONS; WITHDRAWS 2

by Amy Muska-O'Brien, Director UCC Corporate Social Responsibility Ministry



The United Church Foundation advocates for corporate social responsibility (CSR) through security screening, proxy voting, and by filing shareholder resolutions.

- We screen securities out of our portfolio based on the percentage of revenue derived from objectionable activities, such as the manufacture, distribution and/or sale of alcohol, tobacco, and gambling related products.
- We vote our shares at corporate annual meetings consistent with our Social Issues and Corporate

Governance Proxy Voting Guidelines, thus exercising our collective power as shareholders for bettering corporate behavior.

And,

- We file shareholder resolutions that advocate for changes that reflect best practices in corporate social responsibility. In so doing, we bear witness to our faith-based convictions and enable other shareholders to stand with us, as these resolutions reach all shareholders with their annual meeting proxy materials.

This year, the UFC co-filed eight shareholder resolutions. Hundreds of other issues appearing in proxy statements will be voted in accordance with our policy guidelines. To date, the number of social issue proposals filed this year is approaching 300, with environmental issues predominating. Nearly 700 corporate governance proposals have been filed where the highest priority issue is executive compensation, followed by auditor independence. Perhaps the upcoming presidential election explains renewed interest in corporate political contribution issues this year. Equal employment opportunity, and the adoption of sexual orientation anti-bias policies also focus shareholder concern this year.

Although we usually find ourselves in the minority among shareholders on most issues, the last issue of UCFocus described two precedent-setting agreements that were major victories for activists. The withdrawal agreement forged with

American Electric Power, and a similar agreement that has now been made with the Southern Company, reflect a substantial change in attitude about the potential impact of green house gasses not only upon the environment, but also upon their prospects for future corporate profits.

To recap, members of AEP's and Southern's boards of directors have agreed to publish a model report addressing how their companies are responding to increased regulatory pressure to reduce carbon dioxide as well as conventional air pollutants like sulfur dioxide, nitrogen oxides and mercury. These agreements mark the first time that such major carbon-emitting companies have pledged to conduct such a broad risk assessment study and make the results publicly available. Shareholder proponents will be following the progress of these studies closely, and will assess them thoroughly when released.

The CSR Ministry also participated in a number of other negotiations with company leaders over the last

year. No other withdrawal agreements have been negotiated, so proposals that the UCF co-filed will go to vote at Ford Motor Company (May 13th), General Motors (June 2nd), Unocal Corporation (May 24th), Wal-Mart (June 4th), and YUM! Brands (May 20th). Unfortunately, ExxonMobil made a successful case at the Securities and Exchange Commission to have several shareholder proposals omitted from their 2004 proxy statements. But we will continue to work with other co-filers at each company, continuing to call upon corporate managers to be faithful stewards of our collective investment assets.

Observers of shareholder activism often point to the votes shareholder proposals receive at a company's annual meeting and disparage the limited effectiveness of this method of seeking change. However, one goal of the process is to engage senior management in meaningful dialogue over areas of concern, and eventually to help companies make important changes in corporate policy.

Consistent with its investment approach, the UCF's CSR work is long-term by nature and requires patience. We appreciate the steadfast support, encouragement and commitment to this work shown over and over again by our participants. ➤

Editor's note:

On April 19th, Amy gave birth to Aidan Joseph, 10 lbs. 6 oz., 21.5". Mother and baby are fine. Amy will be on maternity leave until July.

BOARD APPROVES 2004 MANAGEMENT FEES

At its semi-annual meeting last February, the UCF Board of Directors approved the following management fees charged to the income earned by the four Common Investment Funds. The UCF Equity Fund -

0.45%; the UCF Balanced Fund - 0.40%; the UCF Fixed-Income Fund - 0.30%; the UCF Cash and Equivalent Fund - 0.10%.

These fees are the only source of funding for the operating costs of the Foundation, and

will now more closely approximate the actual cost of managing each fund. They are close to one-third of the average cost of comparable mutual funds. In 2003, both large cap blend equity funds and moderate allocation funds averaged expense ratios of

1.30% and intermediate-term bond funds averaged 1.09%. Our significantly lower costs enable us to return more of the earnings from your holdings to support your ministry and mission programs. ➤

THOUGHTS UPON RETIREMENT

by George Doty,

Chief Investment Officer,

PB-UCC



It is with a great deal of both joy and sadness that I say goodbye to the churches, agencies, covenanted ministries and other institutions of the United Church of Christ that invest in the Funds of the United Church Foundation, to the hard working employees of the Foundation, and to the wonderfully talented and dedicated investment staff with whom I have worked for the past twelve years. Together we have experienced some of the best times in our country's financial history, as well as some of its most difficult times.

It has been a great privilege for me to have had the opportunity to serve all of you during both the good times and the bad. I have enjoyed every minute of it.

Looking ahead, I am optimistic. While we are not likely to see a return to the extraordinary investment years of the 1980's and 1990's anytime soon, I strongly believe that the worst is now behind us, and that better times lie ahead. We should never underestimate the imagination, the courage, and the flexibility of the people that make up our economy, nor should we fail to appreciate their ability to respond and adapt creatively to changing

circumstances. This is our heritage. We are seeing it played out before our eyes.

If I could share some concluding investment thoughts with you, I would say, stick with your long-term investment plans, maintain broadly diversified portfolios, and don't take unnecessary risk. In my opinion, good investment results over time stem primarily from adhering to these basic investment principals.

Thank you for the opportunity to serve you. I wish you peace and great joy. ➤

EMPLOYEE FOCUS

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of which were based on socially responsible investing (SRI) principles. In general, their investment policies called for diversified, well-balanced portfolios that would allow them to fund their programs while at the same time maintain the purchasing power of their asset base.

UCFocus: How does investing for retirement security differ from investing endowment fund money? Or, to put it another way, do you anticipate needing to do anything different with the funds held for UCC annuitants vs. the funds held for UCF participants?

Kate: I do not anticipate managing the funds differently as I believe both constituencies have been, and will continue to be, well served by a management style that emphasizes total return and prudent risk management along with broad diversification by sector and security.

UCFocus: Given historically low interest rates, and the threat of inflation (and the higher interest rates it may portend), what should we think about bonds right now, as an asset class? Are they still an attractive choice for long-term investors?

Kate: We have most likely seen the low in interest rates for this cycle. Ten-year U.S. Treasury yields have risen approximately 1.2% from the low they reached in June 2002 to about 4.3% currently. We took steps earlier this year to reduce interest rate exposure in the UCF bond portfolio to preserve principal.

It is reasonable to expect that interest rates will trend somewhat higher as the Federal Reserve adjusts monetary policy to keep inflationary pressures under control. If they are successful, then inflation should remain in a range of 1.5% to 3.5% in the next several years, which has been the experience over the last decade. Therefore, we expect interest rates to move in a range of 3.5% to 5.5% over the next several years.

Although investors may experience a decline in their bond portfolio in the short run, over the long-term bonds should continue to provide positive returns. As a long-term investor, I think it is important to remember that an allocation to bonds is important to diversify the risk of a portfolio. In addition, regular coupon income from bonds provides a steady cash flow to fund programs without having to sell assets in a bad market environment.

UCFocus: The UCF Equity Fund has done well in the past without owning enterprises

that, among other things, exploit human weaknesses and addictions, such as smoking, drinking, and gambling. But taken together, don't these very profitable but excluded companies make up a large portion of the gains experienced by our benchmark? Without owning them, can we still outperform the index consistently, or must socially responsible investors pay a price in terms of performance for putting their convictions into practice?

Kate: Actually, these types of enterprises, along with defense, only make up about 3% of the S&P 500 Index, so there are plenty of other stocks to choose from to seek returns in excess of the benchmark. My experience with SRI has been positive. As a fixed income portfolio manager, I managed many accounts that adhered to SRI principles and their performance was in line with non-SRI accounts. During my tenure at Neuberger, the socially responsible equity fund exceeded market benchmarks. Over the long run, SRI principles should not affect our ability to meet or beat the benchmark. One need only look at the record of the UCF Equity Fund to see proof of this. Based on this experience, I would have to say that participants in SRI funds can put their convictions into practice and still expect to earn competitive returns.

UCFocus: From your point of view as an investment management professional, what is the most important thing that investment committees should remember when they deliberate about how best to preserve the real value of their church's assets over the decades, while still drawing income to support the mission of their organizations?

Kate: I believe the most important thing is to stick to an asset allocation policy that results in a long-term, well-diversified balanced portfolio, one that seeks to maximize risk-adjusted returns and then maintains a strict discipline of rebalancing to the policy guidelines when allocations exceed their targets. This should ensure meeting the dual objectives of preserving the real value of their church's assets while providing steady income to support ministry programs over long periods of time.

UCFocus: Thank you for speaking with us, and for taking upon yourself this important responsibility. We look forward to hearing more from you in the future.

Kate: You're welcome. I look forward to getting to know our participants better. ➤

PERFORMANCE & ANALYSIS

INVESTMENT PERFORMANCE

MARCH 31, 2004

For more information on the Common Investment Funds offered by United Church Foundation, call toll-free (877) 806-4989 or visit our website at www.ucfoundation.org

| AVERAGE TOTAL RATES OF RETURN | ANNUALIZED | | | | | | | |
|---|--------------|----------------|--------------|----------------|----------------|---------------|------------|--------------|
| <i>Returns on UCF funds are presented net of fees</i> | Year to Date | 1 Year | 3 Years | 5 Years | 10 Years | Current Yield | Unit Value | Market Value |
| UCF Equity Fund – includes 11.2% international equity <i>S&P 500 Index</i> | 2.4% 1.7% | 36.8% 35.1% | 0.5% 0.6% | -0.4% -1.2% | 11.1% 11.7% | 1.6% | \$9.2073 | \$346.8M |
| UCF Fixed-Income Fund <i>Lehman Brothers Government/Credit Bond Index (LBGC)</i> | 3.0% 3.1% | 5.5% 6.2% | 7.2% 8.0% | 6.9% 7.6% | 7.3% 7.6% | 4.7% | \$4.5332 | \$194.4M |
| UCF Balanced Fund – (63.0% Equity, 37.0% Fixed Income) <i>Strategy Index (See Note)</i> | 2.7% 2.2% | 24.2% 23.7% | 2.5% 3.0% | 2.1% 2.0% | 9.2% 9.6% | 2.7% | \$7.1389 | \$311.8M |
| UCF Cash & Equivalent Fund (annualized) <i>Lipper Money Market Funds Index (annualized)</i> | 0.8% 0.5% | 0.8% 0.5% | 1.4% 1.5% | N/A — | N/A — | 0.9% | \$1.0000 | \$3.6M |
| <i>Consumer Price Index (Inflation) (annualized)</i> | 2.5% | 2.4% | 2.2% | 2.5% | 2.5% | | | |

NOTE: The Strategy Index represents the actual allocation percentages of Fixed-Income and Equity in the Balanced Fund applied to the LBGC and S&P indices.

SECTOR DISTRIBUTION ANALYSIS

| UCF Equity Fund | | | | UCF Fixed-Income Fund | | | |
|-----------------------------|--------------------------------------|----------------|-----------------|-------------------------|--------------------------------------|------------------|--------------|
| Sector | Sector Distribution (% of Portfolio) | | | Sector | Sector Distribution (% of Portfolio) | | |
| | UCF 3/31/04 | S&P 3/31/04 | UCF 12/31/03 | | UCF 3/31/04 | LBGC* 3/31/04 | Difference |
| Consumer Staples | 6.6 | 6.4 | 6.4 | Treasury | 20.0 | 37.5 | -17.5 |
| Consumer Health Care | 13.9 | 13.1 | 13.7 | Agency | 13.2 | 19.4 | -6.2 |
| Media | 4.6 | 3.8 | 4.8 | Mtge-Backed | 2.6 | 0.0 | 2.6 |
| Services | 2.0 | 1.8 | 2.0 | Total Government | 35.8 | 56.9 | -21.1 |
| Retail Stores | 7.9 | 7.8 | 7.4 | Asset-Backed | 8.2 | 0.0 | 8.2 |
| Consumer Durables | 1.6 | 1.7 | 1.5 | Industrials | 20.3 | 20.4 | -0.1 |
| Information Technology | 16.7 | 16.3 | 18.4 | Electric/Gas | 3.6 | 3.6 | 0.0 |
| Industrials | 8.0 | 7.9 | 8.4 | Finance | 20.8 | 12.9 | 7.9 |
| Financials | 21.5 | 21.2 | 20.4 | International | 6.0 | 6.2 | -0.2 |
| Energy | 5.9 | 6.0 | 5.8 | Taxable Munis | 0.8 | 0.0 | 0.8 |
| Materials | 3.1 | 2.9 | 3.2 | Cash | 4.4 | 0.0 | 4.4 |
| Transportation | 1.6 | 1.5 | 1.7 | Total Credit | 64.1 | 43.1 | 21.0 |
| Telecommunications Services | 3.7 | 3.5 | 3.5 | Total Portfolio | 100.0 | 100.0 | |
| Utilities | 2.9 | 2.9 | 2.6 | | | | |
| Miscellaneous | 0.1 | 3.1 | 0.1 | | | | |

*Lehman Brothers U.S. Government/Credit Bond Index

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475 Riverside Drive, Suite 1020
New York, NY 10115

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